STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Illinois Commerce Commission on its own motion	)	
	)	Docket No. 01-0705
Northern Illinois Gas Company d/b/a NICOR Gas Company	)	
Reconciliation of Revenues collected under Gas Adjustment Charges with Actual Costs prudently incurred	)	
Illinois Commerce Commission on its own motion	)	
	)	Docket No. 02-0067
Northern Illinois Gas Company d/b/a NICOR Gas Company	)	
Proceeding to review Rider 4, Gas Cost, pursuant to Section 9-244(c) of the Public Utilities Act	)	
Illinois Commerce Commission on its own motion	)	
	)	Docket No. 02-0725
Northern Illinois Gas Company d/b/a NICOR Gas Company	)	
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NICOR GAS COMPANY'S
REPLY BRIEF

Dated: April 27, 2012

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NICOR GAS COMPANY'S
REPLY BRIEF

In accordance with the schedule established by the Administrative Law Judges ("ALJs"), Northern Illinois Gas Company d/b/a Nicor Gas Company ("Nicor Gas" or the "Company") hereby files with the Illinois Commerce Commission ("Commission") this Reply Brief following evidentiary hearings held on February 28 through March 1, 2012.

I. EXECUTIVE SUMMARY

> "In my testimony, I am *not* accusing Nicor of having acted imprudently or having manipulated anything or any wrongdoing." Testimony of the Illinois Attorney General's Office ("AG") witness David Effron, February 29, 2012, Tr. 1343:1-3 (emphasis added).

* * * *

After a decade of discovery involving more than a dozen depositions, thousands of data requests and the production of hundreds of thousands of pages of material, the AG's only witness in this case testified at evidentiary hearings that he is not accusing Nicor Gas of acting imprudently or of engaging in any wrongdoing with regard to the Company's implementation and operation of the Gas Cost Performance Program ("GCPP"). *Id.* Despite this clear and unambiguous statement from the AG's only witness, the AG's Initial Brief is filled with claims to the contrary. Not surprisingly, the AG's Brief fails to cite to its own witness' testimony to support such claims. The Initial Brief of the Citizens Utility Board ("CUB") likewise is filled with sensational accusations about Nicor Gas' conduct before and during the operation of the GCPP. The allegations of the AG and CUB, however, have nothing to do with the three issues that remain outstanding concerning the GCPP. Instead, the AG and CUB seek to inflame the Commission and divert its attention by making a host of incendiary claims about Nicor Gas and its GCPP—none of which has any evidentiary support.

The facts demonstrate that Nicor Gas' Commission-approved GCPP was in effect for only three years from January 1, 2000 to December 31, 2002. Bartlett Dir., Nicor Gas Ex. 1.0, 5:101-07. The Company acknowledged that accounting errors related to the GCPP were made, and these errors were corrected in filings made with the Commission and the United States Securities and Exchange Commission ("SEC") in 2003. *Id.* at 7:147-8:164. Nicor Gas' actions

associated with the GCPP also were investigated by the United States Attorney's Office for the Northern District of Illinois and a former U.S. Attorney, and neither investigation concluded that Nicor Gas had engaged in fraudulent activity or that it had manipulated its gas storage activities.[1]

In reality, the rhetoric of the AG and CUB relates to issues that have been fully resolved in the Stipulation ("Stipulation") entered into between Commission Staff ("Staff") and Nicor Gas. Nicor/Staff Ex. 1.0. The Stipulation, based on the evidentiary record, resolved all issues as to which Staff asserted that the Company is liable for a refund in this proceeding and, if accepted, would have Nicor Gas refund $64 million to its customers. *Id*. Contrary to the assertions of the AG and CUB, one of the express terms of the Stipulation was agreement between Nicor Gas and Staff that nothing in the Stipulation "constitutes an admission of liability or fault on the part of Nicor Gas." Nicor/Staff Ex. 1.0, ¶ 7.

Notwithstanding CUB's claims, CUB concedes in its Initial Brief—and its witness Jerome Mierzwa admitted at evidentiary hearings—that the Stipulation addressed, in identical or substantially similar amounts, the refunds CUB seeks on the same issues. CUB Init. Br. at 19, 41, 59, 61, 62, 64, 65; Tr. 1109:9-1110:7. Noticeably absent from the AG's Initial Brief is any reference to the Stipulation whatsoever even though the AG now apparently concedes that the Stipulation resolved its claim relating to the benefit of accessing low-cost last-in first-out ("LIFO") layers of gas inventory.

With regard to the three remaining alleged GCPP issues—(1) 2001 Storage Cycle Claims, (2) Storage Carrying Charges, and (3) Delivered Storage Service ("DSS") withdrawals—Nicor Gas has demonstrated that the AG and CUB are wrong on the law and the

[1] Although CUB relies liberally on the report prepared by the investigative team of attorneys and accountants led by Scott Lassar, the former U.S. Attorney for the Northern District of Illinois (*see, e.g.*, Init. Br. at 5, 6, 10, 13, 21-24), CUB conveniently ignores that this team specifically found that Nicor Gas did not engage in "improper attempts to manipulate the storage cycle." CUB Ex. 1.02 Rev. at 52, n.24.

facts. At a bare minimum, the AG and CUB have fallen woefully short of meeting their burden of proof. Turning first to the law, the AG concocts a legal standard that is not found in the Public Utilities Act ("Act") and that also is inconsistent with the Commission's Order approving the GCPP. In approving the GCPP, the Commission expressly determined that Nicor Gas' actions under the GCPP would not be subject to a prudence review and, in fact, the Commission approved tariffs to that effect. Further, contrary to the AG's claim, nothing in Section 9-244 of the Act suggests that the Commission should engage in a hindsight review of the performance of an alternative regulation plan for purposes of making retrospective changes to the plan and its results. Similarly, CUB's attempt to impose prudence standards on the Company's gas purchasing activities also is misplaced. And, ordering refunds in connection with CUB's adjustment relating to storage carrying charges would constitute improper single-issue and retroactive ratemaking. *See, e.g., Citizens Util. Bd. v. Illinois Commerce Comm'n*, 166 Ill. 2d 111, 136-37 (1995); *Citizens Utilities Co. v. Illinois Commerce Comm'n*, 124 Ill. 2d 195, 210-11 (1988).

The AG and CUB also are wrong on the facts. First and foremost, they have not presented any competent evidence to support their claims. And, even assuming some type of prudence review was appropriate, which it is not, neither the AG nor CUB witness present any facts to support claims concerning Nicor Gas' 2001 storage cycle. Not only are their assertions based upon assumptions or inferred "facts," such "hypothetical world" claims are contradicted by real world explanations. Meanwhile, CUB's claims concerning storage carrying costs and DSS withdrawals are unrelated to the GCPP and/or unfounded, as described in detail below.

Finally, the proposal made by the Retail Energy Supply Association ("RESA") and Interstate Gas Supply of Illinois, Inc. ("IGS") concerning how any refund should be allocated to

customers lacks evidentiary support. Although they had the opportunity to do so, neither RESA nor IGS submitted any testimony to support their proposal. Rather, they first articulated the proposal in their Initial Brief. Thus, no party had the opportunity to evaluate the proposal and determine whether it would impose any unreasonable costs or administrative burdens on the Company. For these reasons, Nicor Gas continues to support Staff's recommended refund methodology.

II. APPLICABLE STATUTORY AUTHORITY

The AG and CUB properly recognize that the Commission's review of the GCPP in these consolidated proceedings is governed by Section 9-244 of the Act; however, their Initial Briefs incorrectly rely on subsections (a) and (b) of that statute. *See*, *e.g.*, AG Init. Br. at 9-10; CUB Init. Br. 9, 34. Instead, the Commission's review here is governed by subsection (c), which provides in its entirety as follows:

> The Commission shall open a proceeding to review any program approved under subsection (b) 2 years after the program is first implemented to determine whether the program is meeting its objectives, and may make such revisions, no later than 270 days after the proceeding is opened, as are necessary to result in the program meeting its objectives. A utility may elect to discontinue any program so revised. The Commission shall not otherwise direct a utility to revise, modify or cancel a program during its term of operation, except as found necessary, after notice and hearing, to ensure system reliability.

220 ILCS 5/9-244(c). Thus, contrary to the arguments of the AG and CUB, nothing in Section 9-244 authorizes the hindsight review they claim the Commission now should conduct—either of the proceeding in which the GCPP was approved[2] or the Company's actions under the GCPP. Instead, Section 9-244(c) directs the Commission to review the Company's performance under

[2] Interestingly, the AG argues at length in its Initial Brief about Nicor Gas' actions in the proceeding in which the Commission approved the GCPP even though the AG did not appear or participate in any way in that proceeding.

the GCPP solely for the purpose of making revisions to the program on a prospective basis. Indeed, under the express language of the statute, the utility may choose to reject any changes to the program made by the Commission and discontinue it going forward.

Moreover, in approving the GCPP, the Commission specifically recognized that the Company's actions under the GCPP are not subject to a *post hoc* prudence review under Section 9-244:

> Instead of the traditional prudence review, Section 9-244(c) requires that the Commission review the program two years after its implementation to determine whether it is meeting its objective.

Docket No. 99-0127, Order at 37 (Nov. 23, 1999). This standard of review also is reflected in Nicor Gas' Commission-approved tariffs, which state, in pertinent part: "The Commission shall not consider the prudence of gas costs incurred for any period included in Rider 4, Gas Cost Performance Program." Ill. C. C. No. 16-Gas, 3rd Revised Sheet No. 62.

III. CONTESTED ISSUES

Although the AG and CUB steadfastly maintain their grossly inflated refund requests for hundreds of millions of dollars (AG Init. Br. at 38; CUB Init. Br. at 67)—even in the face of the Stipulation between Nicor Gas and Staff—their Initial Briefs fail to present any evidence to rebut Nicor Gas' showing that their proposed adjustments are contrary to applicable law, the facts, or both. Instead, the AG and CUB try to sensationalize their claims in an attempt to persuade the Commission to order far more in customer refunds than Staff ever has advocated for or has agreed in the Stipulation is reasonable. At the same time, the AG and CUB concede that the Stipulation resolved most of the issues that were originally contested, leaving just three alleged GCPP issues for resolution by the Commission. Because they are wholly unsupported by the evidentiary record and are not required by any law, the Commission should reject each of the

remaining contested issues: (1) the AG's and CUB's claims concerning Nicor Gas' 2001 storage cycling; (2) CUB's claim concerning alleged storage carrying charges; and (3) CUB's claim regarding DSS storage withdrawals.

A. LIFO Benefit

As demonstrated in Nicor Gas' Initial Brief, the Stipulation between Nicor Gas and Staff fully addresses this issue and Nicor Gas will refund $21,871,934, which is the amount claimed by Staff to represent 100% of the LIFO benefit. Nicor Gas Init. Br. at 13, 16. Staff provides additional argument in support of the Stipulation as to this issue in its Initial Brief. Staff Init. Br. at 5-6.

Importantly, it appears that the AG concedes in its Initial Brief that the Stipulation between Nicor Gas and Staff fully addresses this issue even though the AG originally proposed a higher adjustment than the amount claimed by Staff to represent 100% of the LIFO benefit. Specifically, the AG no longer advocates for a refund of $25,156,000 associated with the LIFO benefit and limits its refund request to the amounts it ascribes to the 2001 storage issue. AG Ex. 1.3 Rev., Sch. DJE-7; AG Init. Br. at 38.

The AG's concession on this issue leaves CUB alone to pursue a higher refund than that agreed to between Staff and Nicor Gas. And in order to support its solitary claim, CUB raises several inflammatory—and speculative—arguments about Nicor Gas' conduct in the proceeding in which the GCPP was approved and in these consolidated proceedings. CUB Init. Br. at 26-28. For example, CUB argues that Nicor Gas employees "revealed in their depositions a strategy to conceal its intentions to liquidate its low-cost LIFO inventory." *Id*. at 27. Yet, as Nicor Gas has repeatedly pointed out in this proceeding, CUB improperly relies on isolated excerpts from the

discovery depositions of Nicor Gas employees that are taken out of context.[3] *See, e.g.*, Nicor Gas Motion to Strike filed October 9, 2009. To place CUB's excerpts into context, Nicor Gas introduced into evidence counter-designated deposition testimony excerpts from deponents who were executives and management connected to the GCPP or the gas cost supply reconciliations that are the subject of these proceedings. Contrary to CUB's claims (Initial Brief at 27), Nicor Gas' counter-designated excerpts below demonstrate that the Company had neither a "strategy to conceal" nor "intentions to liquidate its low-cost LIFO inventory."

- Philip Cali, former Executive Vice President of Operations, testified that at the time the Company made its GCPP filing with the Commission in 1999, the Company intended to generate savings "[b]y managing its supply acquisition and supply-related assets very differently than we had ever done in the past." Nicor Gas Ex. 19.0 at 56:20-57:2. More specifically, the Company conceived of numerous strategies to generate savings, including (i) "getting third parties who had a broader regional knowledge of supply marketplace in the midwest to assist us with managing our pipeline contracts and our lease storage activities"; (ii) getting "assistance in managing our on-systems storage facilities in a very different way from what we traditionally did in the past"; (iii) "set[ting] up new systems within the company to monitor what financial derivative products we were going to be employing in the acquisition of gas supplies and the acquisition of pipeline capacity." *Id*. at 57:3-58:3.

- Mr. Cali also testified that no one at the Company, at any point in time, "indicate[d] that they considered one of the main purposes of the PBR was to tap into the low-cost LIFO layers[.]" Nicor Gas Ex. 19.0 at 66:18-67:5.

- Leonard Gilmore, then Manager of Pipeline Regulation and Supply Planning, testified that "the purpose of the PBR was not to access the low-cost inventory"; instead, "[i]t was to perform under the benchmark." Nicor Gas Ex. 17.0 at 24:10-13, 25:20-26:7.

[3] Indeed, CUB even misleadingly describes the excerpts it cites. For example, CUB argues that Mr. Harms testified that "had the Commission known about the Company's plans to access LIFO layers, 'there was a good chance they would approve a PBR, but my belief is that the sharing percentages might have changed.'" CUB Init. Br. at 27-28, 34. However, the actual question posed to Mr. Harms was "whether the Commission would have approved the PBR in the same form that it was approved in '99 had it known that the LIFO layers—had it known about the LIFO layers?" Mierzwa Dir., CUB Ex. 1.0 2nd Rev., 26:702-16. Thus, the phrasing about the Company's supposed "plans to access LIFO layers" is CUB's alone, not that of Mr. Harms.

- Albert Harms, former Manager of Rate Research, testified that the Company never "anticipated anything like manipulation" of its gas storage. Nicor Gas Ex. 13.0 at 24:8-11.

- Mr. Harms also testified that the Company had "no plan to release LIFO gas" at the time the inventory value report was done and the GCPP was approved by the Commission. Nicor Gas Ex. 13.0 at 200:4-11.

- Beth Hohisel, former Manger of Supply Services, testified that she "was aware that LIFO was a possibility within the PBR, but that was not the intent of it." Nicor Gas Ex. 15.0 at 188:14-20.

- Theodore Lenart, former Assistant Vice President of Supply Operations, testified that, at the time the GCPP filing was made, the Company "intended to generate savings" through "the various benchmarks that were imbedded in the PBR, including storage, transportation, and commodity, we could profit under any and all of those." Nicor Gas Ex. 18.0 at 27:6-12

- Mr. Lenart also testified that accessing the LIFO layers "was not part of the supply operations goals" whose goals were "to beat the benchmark with the tools that were at our disposal." Nicor Gas Ex. 18.0 at 28:4-9.

- Mr. Lenart further testified that the Company "did not look at the LIFO as the reason for doing the PBR" as the Company "fully intended to and did aggressively manage [its] business to try to derive value, without regard to the LIFO layer." Nicor Gas Ex. 18.0 at 63:14-64:2.

The problems inherent in CUB's selective use of discovery deposition transcript excerpts as supposed "proof" in support of its claims are further highlighted by the fact that CUB failed to take any steps whatsoever to call a single witness to testify at the evidentiary hearings other than its own expert Mr. Mierzwa. For example, in response to an inquiry by the ALJ, CUB's counsel admitted that CUB did not make any attempt to get Mr. Harms to participate in the evidentiary hearings. Tr. 1484:16-20. So although CUB at one time specifically contemplated calling adverse witnesses and issuing subpoenas to have those individuals appear at the evidentiary hearings, those steps were indisputably not taken. Tr. 1485:18-1486:4. Instead of making the effort, CUB resorts to reliance on the deposition transcript excerpts and thinly veiled criticism of

Nicor Gas for offering only one witness who worked at the Company at the time of the GCPP who testified that he had no involvement in discussions regarding the GCPP. CUB Init. Br. at 17-18.

Finally, even though CUB argues that its proposed LIFO adjustment is "more appropriate" than the adjustment supported by Staff witness Zuraski and adopted in the Stipulation (CUB Init. Br. at 26), CUB actually cites to Mr. Zuraski's pre-filed testimony as support for its higher adjustment based upon a different methodology. CUB Init. Br. at 26, 29. The Commission should approve the refund agreed to in the Stipulation and reject CUB's unsupported request for a higher amount.

B. Storage Carrying Charges

As an initial matter, Nicor Gas emphasizes that this adjustment proposed by CUB is unrelated to actions taken during the period the GCPP was in effect, 2000-2002, but, instead, relates to actions in 2003. Thus, this issue is unrelated to the GCPP.

CUB is alone in advocating for a more than $40 million refund related to the higher carrying charges associated with replacing low-cost LIFO layers with higher cost layers as neither the AG nor Staff proposed such a refund and neither party ever supported CUB's claim. That is not surprising given that CUB's claim is not supported by the Act, the Commission's Rules, or the evidentiary record. Indeed, CUB witness Mierzwa freely admitted that this $40 million refund would only be appropriate "if the Commission wanted to punish Nicor" Gas. Tr. 1237:11-15. But the Commission has no authority to award punitive damages, and CUB cites to no such authority.

The only legal support cited by CUB for its position is Section 9-244(b)(1) of the Act. CUB Init. Br. at 34. However, that subsection of the Act pertains to the initial, forward-looking approval of a utility's performance-based regulation program, not the review that is at issue here

under Section 9-244(c). In addition, CUB's adjustment is completely inconsistent with the Commission's acceptance of the LIFO methodology of accounting for gas in storage, which implicitly recognizes that additional layers will be added to storage inventory with different prices. *See, e.g.*, 83 Ill. Adm. Code 505.1170(C). And nothing in the Act or the Commission's Rules prohibits a utility from using gas in inventory. Staff witness Richard Zuraski agreed to this point. Tr. 1284:12-15. Further, nothing in the Act or the Commission's Rules prohibits a utility from adding a LIFO layer of gas that is priced higher than a previous layer of gas. Again, Staff witness Zuraski agreed to this point. Tr. 1284:7-11. In addition, nothing in the Act or the Commission's Rules even suggests that a utility should be penalized when it adds a LIFO layer of gas that is priced higher than prior layers. To the contrary, utilities routinely include in rate base higher cost assets that replace lower cost, depreciated assets.

Moreover, permitting CUB's proposed adjustment on this point would require the Commission to re-calculate rates that it previously found just and reasonable in prior Nicor Gas rate cases. In Nicor Gas' 2004 rate case, the Commission found Nicor Gas' valuation of gas in storage, which included the cost of the 2003 incremental LIFO layer (the layer targeted by CUB), just and reasonable. Docket No. 04-0779, Order at 19 (Sept. 20, 2005). *See also* Docket No. 08-0363, Order (Mar. 25, 2009 and Oct. 7, 2009). To order refunds as CUB proposes would constitute improper single-issue and retroactive ratemaking. *See, e.g., Citizens Util. Bd. v. Illinois Commerce Comm'n*, 166 Ill. 2d 111, 136-37 (1995) ("The rule against single-issue ratemaking … prohibits the Commission from considering changes to components of the revenue requirement in isolation. Consideration of any one item in the revenue formula in isolation risks understatement or overstatement of the revenue requirement.") (citations omitted); *Citizens Utilities Co. v. Illinois Commerce Comm'n*, 124 Ill. 2d 195, 210-11 (1988) ("Allowing the rate

base reduction to stand would sanction retroactive ratemaking, a practice that this court has long condemned as inconsistent with the statutory scheme and the Commission's role in the ratemaking process.").

CUB ultimately concedes that the basis for its proposed refund is "Nicor's imprudent decision to liquidate LIFO layers outside regulatory purview." CUB Init. Br. at 34. Yet, the imposition of a prudence standard is legally improper in a performance-based regulation context. *See*, *e.g.*, Docket No. 99-0127, Order at 37 (Nov. 23, 1999) (citing Section 9-244 of the Act). And, even if prudence was an appropriate standard in this case, CUB utterly failed to support its claim that Nicor Gas acted imprudently in accessing the low-cost inventory. Carpenter Reb., Nicor Gas Ex. 5.0R, 26:492-27:507.

C. DSS Withdrawals

Yet again CUB stands alone in arguing that the Commission should refund $8,149,519 related to Nicor Gas' DSS storage withdrawal activity.[4] CUB Init. Br. at 35-39. The AG neither proposed this refund nor supported CUB's claim, and Staff withdrew its claim on this issue. Nicor/Staff Ex. 1.0, ¶ 4.

Nicor Gas demonstrated that it already has corrected (in its restated GCPP results) the prior treatment of its December 1999 sale/release of DSS to IMD Storage Management and Asset Transportation Company to account for its use of DSS (and NSS) storage between 2000 and 2002, and those restatements were accepted by Staff and Intervenors. Carpenter Reb., Nicor Gas Ex. 5.0R, 10:187-89, 35:671-72, 36:685-87. Indeed, Nicor Gas' restated results were ratified by Nicor Gas' outside independent auditors and were accepted by the SEC. Carpenter

[4] Nicor Gas leases DSS capacity from a third party, Natural Gas Pipeline Company of America. DSS is not part of Nicor Gas' system of Company-owned aquifer storage fields.

Sur., Nicor Gas Ex. 10.0, 24:459-61; *see also* Tr. 1231:6-20 (Mierzwa). Importantly, the Company has never offered further revisions to its restated financials throughout the course of these extended proceedings.[5]

CUB argues that "[b]ecause the Company did not address the merits of CUB's adjustments directly in its surrebuttal testimony, the Commission should reject the Company's claim that all DSS storage volumes have been properly reclassified in the Company's restatements, and adjust Nicor's PBR performance to account for all physical DSS withdrawals as proposed by CUB." CUB Init. Br. at 38. CUB is mistaken. Nicor Gas witness Dr. Carpenter addressed Mr. Mierzwa's DSS withdrawal claim at pages 22 to 25 of his surrebuttal testimony under the heading "Additional DSS Withdrawals." Carpenter Sur., Nicor Gas Ex. 10.0, 22:410-25:463. Indeed, in his surrebuttal testimony, Dr. Carpenter expressly discusses the two documents CUB argues he ignored (Init. Br. at 37) and explains that they do not support Mr. Mierzwa's claim. *Id*. at 23:422-24:459. Instead, the documents show that Mr. Mierzwa merely relies on a discrepancy in the amount of DSS withdrawals reflected between them: one (NIC 114180) showing 7.2 million MMBtu DSS withdrawals more than the other (NIC 109409). *See*, *e.g.*, Mierzwa Dir., CUB Ex. 1.0 2nd Rev., 40:1123-41:1151; CUB Ex. 1.12. Although CUB never explains why, Mr. Mierzwa selects the higher figure even though Nicor Gas and its auditors obviously rejected reliance on that document. Instead, the figures shown in NIC 109409 (Nicor Gas Ex. 10.2), which was used for the restatement, represent Nicor Gas' actual physical DSS withdrawals.

Dr. Carpenter also points to other documents provided in discovery to CUB that support Nicor Gas' treatment of DSS storage withdrawals. Carpenter Sur., Nicor Gas Ex. 10.0, 24:453-

[5] The restated financials remained the same even after the 2004 terminations CUB highlights. CUB Init. Br. at 15.

57; Nicor Gas Exs. 10.3 and 10.4. Nicor Gas' contemporaneous Aquifer Reports, which are excerpted in Nicor Gas Ex. 10.3, show DSS withdrawals that confirm those shown on NIC 109409. In addition, the figures shown in NIC 109409 correspond to the DSS withdrawals shown on other Nicor Gas documents relating to DSS injections and withdrawals in the relevant timeframe. These documents—NIC 114182 and NIC 114183—are in the record at Nicor Gas Exhibit 10.4. Given this evidence, Nicor Gas witness Dr. Carpenter testified in his surrebuttal testimony that Mr. Mierzwa did not justify his claim that the difference he identified between two documents should be used to adjust Nicor Gas' restated results. Carpenter Sur., Nicor Gas Ex. 10.0, 24:447-57. In light of the contrary evidence submitted by Nicor Gas, CUB's unsubstantiated adjustment relating to DSS withdrawals should be rejected.

D. In-Field Storage Transfers

As demonstrated in Nicor Gas' Initial Brief, the Stipulation between Nicor Gas and Staff fully addresses this issue and Nicor Gas will refund $11,149,901. Nicor Gas Init. Br. at 13, 20. Staff provides additional argument in support of the Stipulation as to this issue in its Initial Brief. Staff Init. Br. at 7. CUB concedes that the refund is "the same as CUB's proposed adjustment" and supports Commission approval of the refund agreed to in the Stipulation. CUB Init. Br. at 41.

E. 2001 Storage Withdrawals: Intervenors Have Failed To Make Any Showing Justifying Any Relief With Respect To Their Claims Regarding The 2001 Withdrawal Cycle

On the issue of the 2001 reduced withdrawals and increased purchases, one fact is clear: no one who testified in this case really knows why 2001 withdrawals were as low as they were. It is not true, as CUB asserts, that "the Company[] … claim[s] … that the significantly reduced storage withdrawals *were* simply due to weather and operational concerns." CUB Init. Br. at 7 (emphasis added). Nor is it true, as the AG insists, that "Dr. Carpenter *would have the*

Commission believe that much colder weather in November and December 2000 led the Company to withdraw more gas in those months." AG Init. Br. at 27 (emphasis added). None of Nicor Gas' external witnesses—Dr. Carpenter, Mr. Moes, or Mr. Gulick—claims to *know* that as a *fact* and presumably Messrs. Effron and Mierzwa would admit, as they must, that they do not *know* the reason for the low withdrawals either.

Nor have the AG and CUB, despite the overblown claims in their Initial Briefs, provided "extensive evidence" to support their claims. *See, e.g.*, CUB Init. Br. at 42. Although CUB dismisses Nicor Gas' witnesses as "paid consultants" with no "direct personal knowledge or experience regarding implementation of the GCPP" (CUB Init. Br. at 16), it is abundantly clear that Messrs. Effron and Mierzwa at least equally lack such knowledge or experience. Indeed, given the weakness of the AG and CUB "proof" on this issue and the lack of any evidence to support it, the relief requested should and must be denied even without regard to the contrary evidence presented by Nicor Gas.

Everyone does seem to agree why withdrawals, at least in January 2001, were so low, and that is because inventories were so low at the end of 2000. *See, e.g.*, AG Init. Br. at 25 ("There is no dispute that the low inventory level at the end of 2000 was a contributing factor to the low level of withdrawals in 2001."); CUB Init. Br. at 53 ("Because NGPL storage injections were reduced, NGPL contract storage inventory levels were reduced, requiring Nicor to reduce storage withdrawals in January 2001 and its planned annual storage cycle from 87 Bcf in 2000, to 60 Bcf in 2001 (as of January 2001)."). The real disagreement focuses on *why* those inventory levels were so low. And, lacking any first-hand direct evidence in the record, this is a matter of inference. The CUB and AG witnesses claim (though they do not know) that this was because of

Nicor Gas' attempts to access low-cost LIFO inventory. Nicor Gas' witnesses testify that other explanations for these low inventories are far more plausible.

It would be a huge stretch, and unlawful in any event, for the Commission to order refunds in *any* amount—much less amounts approaching $200 million or more—simply on the basis of inference alone. As is well known, the Public Utilities Act requires that a Commission order based on findings that are not supported by "substantial evidence" is subject to judicial reversal. 220 ILCS 5/10-201(e)(iv)(A); *Citizens Util. Bd. v. Illinois Commerce Comm'n*, 166 Ill. 2d 111, 132-33 (1995) (concluding that deference was not owed to "the Commission's policy decision regarding treatment of coal-tar cleanup expenses" "without substantial evidence in the record to support its decision"). *See also Airport Shuttle Service, Inc. v. Interstate Commerce Comm'n*, 676 F.2d 836, 840 (D.C. Cir. 1982) (recognizing that "a decision is not supported by substantial evidence unless there is such relevant evidence as a reasonable mind might accept as adequate to support a conclusion" and finding that there was no such evidence in "routine, laconic, and untested responses to … standardized questions") (internal quotation marks and citations omitted).

The testimony of witnesses lacking any first-hand knowledge of the events in question, based solely on their inferences from a handful of documents, cannot be considered substantial evidence. The AG's Initial Brief does not cite a single contemporaneous document or testimony by any knowledgeable witness to support its claims concerning the 2001 withdrawal cycle. Indeed, its two critical assertions are supported by no record citation whatsoever:

- "Nicor based its gas storage management decisions on beating the benchmark cost of gas, regardless of the impact of those decisions on the costs of gas passed on to consumers." AG Init. Br. at 20-21.

- "In January of 2001, Nicor faced a defining choice: it could have maintained a withdrawal cycle to take advantage of the high SCR, thereby keeping gas costs low

> for its customers but risking underperforming against the benchmark, thereby keeping gas costs low for its customers, or it could ignore the high SCR and suppress its withdrawals to beat the benchmark, thereby raising gas costs for consumers. It chose the latter." AG Init. Br. at 24.

Similarly, CUB's Initial Brief cites neither any contemporaneous document nor witness testimony (other than that of its "paid consultant") to support its central proposition: "Witness Mierzwa found that Nicor deliberately manipulated the use of storage by reducing NGPL contract storage injections in 2000 to access low-cost LIFO layer storage." CUB Init. Br. at 53. Although CUB does cite a handful of contemporaneous documents, those all relate to peripheral and unexceptional "issues,"[6] and not a single one tends to support an inference that Nicor Gas' withdrawals were intended to access low-cost LIFO.

Reliance on mere inference is especially improper when the conclusion inferred by the AG and CUB—that Nicor Gas' greater year 2000 withdrawals were designed to access low-cost LIFO inventory—is in no way wrongful or improper behavior. But in this case, even that inference as to Nicor Gas' motivation cannot be credited because it is far less plausible than other explanations of the low inventory situation. The evidence that renders the AG/CUB inference implausible and unacceptable includes:

- Every gas utility nationwide was faced with a low inventory situation at the end of 2000/early 2001. *See* Nicor Gas Init. Br. at 21-22, 30-31, 33-41.

- These low inventories resulted from a combination of severe cold and resulting increased (and increasing) prices that led gas utilities to draw down their inventories to avoid market purchases of higher priced gas. The United States Energy

[6] *E.g.*, CUB Init. Br. at 51 citing CUB Exs. 1.15 and 2.07 for the position that Nicor Gas "monitored on a daily basis its performance under the Market Index Cost calculation, including the impact of daily changes in natural gas prices"; CUB Ex. 2.08 for the position that "[i]n a month of rising prices, Nicor's PBR Purchasing Guidelines indicated that the Company should buy less gas." Even if these documents reflect the positions for which they are cited, it should hardly come as a surprise, or be deemed evidence of improper behavior, that Nicor Gas closely monitored its performance under the GCPP or reduced gas purchases in a month of rising prices. Indeed, a *failure* to do either of those things might be considered more suspicious.

Information Administration noted in this regard: "Rising prices at the beginning of the natural gas storage refill season in April 2000 resulted in lower levels of injections than normal and unusually low levels of natural gas in storage at the start of the 2000-2001 winter. …the 2000-2001 heating season began with relatively cold temperatures in November and December 2000. The frigid temperatures caused a surge in demand that led to soaring prices and a rapid drawdown of storage levels. …With inventory levels well below expected norms, concerns emerged that they might not be sufficient to last through the heating season." U.S. Natural Gas Markets: Mid-Term Prospects for Natural Gas Supply," United States Energy Information Administration (December 2001), quoted in Carpenter Reb., Nicor Gas Ex. 5.0R, 18:342-19:384; *see* also Carpenter Sur., Nicor Gas Ex. 10.0, 13:234-37 ("At the end of December 2000, U.S. gas storage inventories were much lower than normal, as shown below in Figure 4.[7] Therefore, Nicor Gas was in a position that was comparable to the position of gas consumers nationwide.").

- At the end of October 2000, Nicor Gas' inventory levels were near normal.[8] *See* Nicor Gas Init. Br. at 21, 31. Had Nicor Gas been reducing physical inventory to facilitate access to low-cost LIFO, why did it wait until November 2000 to begin to do so? CUB recognizes that Nicor Gas' preliminary gas supply plan for November 2000 contemplated average withdrawals. CUB Init. Br. at 49-50. Clearly, some unexpected event intervened to upset that calculus. Remarkably, CUB finds something sinister in the decision of Nicor Gas to reduce its purchase of gas in a month of rising prices. CUB Init. Br. at 51. Although CUB says this was done to gain a benefit, it never explains what that benefit was.

- Nicor Gas had no need to rely on physical withdrawals from inventory to access low-cost LIFO. The storage prefill accounting strategy, which allowed Nicor Gas to maintain proper levels of physical inventory without reflecting that physical inventory on its books, was the method chosen to do so. *See* Nicor Gas Init. Br. at 33-34.

- If Nicor Gas were bound and determined to reduce physical inventory levels to access low-cost LIFO, then why did it abruptly reverse that course in 2001 and reduce its withdrawals—especially after January 2001, a point at which Mr. Effron claims (albeit incorrectly) that Nicor Gas' inventory levels were "back to normal." This is a fundamental inconsistency and flaw in their "inference" that AG and CUB never confront: if greater withdrawals were the key to Nicor Gas' core strategy of unlocking low-cost LIFO, why then did it abandon that strategy in 2001 and begin to preserve

[7] Figure 4 was reproduced in Nicor Gas' Initial Brief at 40.

[8] Although CUB attempts to make much of the fact that NGPL inventory levels at the end of October 2000 were substantially lower than average (CUB Init. Br. at 52-54), that fact is irrelevant. What matters is *total* inventory, and that was at a normal level.

inventory unnecessarily? Only one answer exists: withdrawals were never affected by a desire to access low-cost LIFO, not in 2001 and not in 2000.[9]

- The effects of the low year-end 2000 inventory levels continued to be felt after January 2001. Despite Mr. Effron's assertions to the contrary, Nicor Gas' inventory levels at the end of January 2001 were in fact substantially lower than in any other year for which the record contains evidence:

Year	Inventory (Bcf) (End of January)
2001	56.2
2000	65.5
1999	76.2
1998	81.8
1997	73.3
Average 1997-2000	74.2

  Tr. 1360:6-1362:18. On average, then, the inventory levels at the end of January for the four years preceding 2001 were 74.2 Bcf – or 17.4 Bcf (more than 30%) higher than in 2001. And although Mr. Effron agrees that a number of factors other than inventory levels affect the ability to rely on storage withdrawals (Tr. 1358:18-1359:4), his analysis does not address any of those other factors.

- Although CUB relies on Staff's "concerns" in Docket No. 99-0127 that Nicor Gas could shift withdrawals to "create false savings" (CUB Init. Br. at 44) and benefit itself and increase cost to customers, apparently as evidence that is what occurred, Staff never supported or advanced the 2001 storage cycle issue despite Staff's aggressive position on other issues in this proceeding.

- Although CUB and the AG rely extensively on the Lassar Report to support their claims, they fail to note that on this particular issue, the Lassar Report found no evidence that the 2001 storage activity was the result of any improper manipulation. CUB Ex. 1.02 Rev. at 52, n.24. Indeed, Mr. Effron admitted that he is not testifying that Nicor Gas "acted imprudently" or committed "any wrongdoing." Tr. 1343:1-3.

[9] The AG and CUB are likely to claim that the minimization of withdrawals in 2001 was due to a concern that, because of the high Storage Credit Rate ("SCR") in 2001, greater withdrawals would substantially increase the Storage Credit Adjustment ("SCA") and correspondingly lower the benchmark. At that point, Nicor Gas would have had to perform the complicated calculation whether, on a net basis, it was better off (1) increasing physical withdrawals (and accessing low-cost LIFO), or (2) decreasing withdrawals to reduce the SCA and increase the benchmark. If Nicor Gas had performed that calculus, Mr. Mierzwa was apparently unable to locate it in the 360,000 documents he says he reviewed because no evidence of it appears in the record. And, if Nicor Gas had performed that calculation, it apparently chose the wrong alternative, because Mr. Mierzwa's analysis shows that the reduced withdrawals in 2001 increased the cost of gas by more than they increased the benchmark, resulting in a $42.304 million *loss* to Nicor Gas. *See* CUB Ex. 1.18.

In short, the record makes it impossible for any objective, neutral observer to draw the inferences the AG and CUB ask the Commission to draw.

The absence of any basis for CUB's claim is further exemplified by its desperate attempt to prove that Nicor Gas' provision of so-called "hub services" somehow was part of the overall plot to benefit itself to the detriment of its customers and contributed to the "high" gas costs in 2001. CUB points to two transactions.

The first transaction was Nicor Gas' acceptance of 13.7 Bcf of third-party gas into storage in the summer of 2000 and the return of that gas in the winter of 2001. CUB seems to argue first that acceptance of this gas somehow prevented Nicor from storing in its storage facilities gas for its customers' use. CUB Init. Br. at 56 ("Thus, 13.7 Bcf of storage on-system was unavailable to serve sales customers during the winter of 2000-2001."). Alternatively, CUB seems to argue that Nicor Gas should not have returned this gas to the third-party, but should have expropriated it for the benefit of its sales customers. *Id*. ("[B]ecause Nicor was required to return 13.7 Bcf….").

Both arguments border on the frivolous. No evidence shows that, in late 2000, Nicor Gas lacked storage capacity that prevented it from purchasing and storing additional gas had it been economically advantageous to do so. The suggestion that Nicor Gas somehow acted improperly by returning this gas to the third-party requires no comment.

The second transaction that CUB points to appears to relate to separate wholly unidentified transaction(s) in February and March 2001, in which Nicor Gas supposedly loaned 8 Bcf of gas to unidentified third parties, which allegedly shows that Nicor Gas "could have withdrawn more gas from storage to serve sales customers than it did." *Id*. at 57. Neither Mr. Mierzwa nor CUB presented any information about these transactions, or documentation

relating to them, that would explain anything about those transactions including the reason(s) for them (if in fact they existed) or how Nicor Gas customers may have been benefitted by these transactions. Nor has CUB presented any evidence that suggests how this transaction contributed to the tens of millions of dollars that CUB claims must be refunded to customers. In the absence of such information, it would be entirely impermissible to order any relief based on these "transactions."

The AG and CUB have failed to present a shred of competent evidence that would even remotely justify the award of any relief with respect to the 2001 storage withdrawal cycle claims. For all the reasons set forth in Nicor Gas' Initial Brief and in this Reply Brief, the Commission should dismiss all of the AG and CUB claims based on the 2001 withdrawal cycle and deny all relief requested with respect thereto.

F. Tennessee Gas Pipeline and Midwestern Gas Transmission Capacity Costs

As demonstrated in Nicor Gas' Initial Brief, the Stipulation between Nicor Gas and Staff fully addresses this issue and Nicor Gas will refund $1,475,267. Nicor Gas Init. Br. at 13, 41-42. Staff provides additional argument in support of the Stipulation as to this issue in its Initial Brief. Staff Init. Br. at 8-9. CUB concedes that the refund is "essentially the same as CUB's proposed adjustment" and supports Commission approval of the refund agreed to in the Stipulation. CUB Init. Br. at 59.

G. Capacity Management Credits

As demonstrated in Nicor Gas' Initial Brief, the Stipulation between Nicor Gas and Staff fully addresses this issue and Nicor Gas will refund $5,893,472 for the years 2000-2002 and $3,216,169 for the year 1999. Nicor Gas Init. Br. at 13, 42. Staff provides additional argument in support of the Stipulation as to this issue in its Initial Brief. Staff Init. Br. at 9-10. CUB

concedes that the refunds are "the same as CUB's proposed adjustment" and supports Commission approval of the refunds agreed to in the Stipulation. CUB Init. Br. at 61, 62.

H. Affiliate Below Market Sale

As demonstrated in Nicor Gas' Initial Brief, the Stipulation between Nicor Gas and Staff fully addresses this issue and Nicor Gas will refund $4,258,586. Nicor Gas Init. Br. at 13, 42. Staff provides additional argument in support of the Stipulation as to this issue in its Initial Brief. Staff Init. Br. at 10-11. CUB concedes that the refund is "the same as CUB's proposed adjustment" and supports Commission approval of the refund agreed to in the Stipulation. CUB Init. Br. at 64.

I. Aquila Weather Insurance

As demonstrated in Nicor Gas' Initial Brief, the Stipulation between Nicor Gas and Staff fully addresses this issue and Nicor Gas will refund $2,057,525. Nicor Gas Init. Br. at 13, 43. Staff provides additional argument in support of the Stipulation as to this issue in its Initial Brief. Staff Init. Br. at 11-12. CUB concedes that the refund is "substantially similar to CUB's proposed adjustment" and supports Commission approval of the refund agreed to in the Stipulation. CUB Init. Br. at 65.

J. Hub Revenues

As demonstrated in Nicor Gas' Initial Brief, the Stipulation between Nicor Gas and Staff fully addresses this issue and Nicor Gas will refund $6,150,917. Nicor Gas Init. Br. at 13, 43-44. Staff provides additional argument in support of the Stipulation as to this issue in its Initial Brief. Staff Init. Br. at 12-13. Although CUB never made any proposal related to this issue, CUB supports Staff's proposed adjustment and Commission approval of the refund agreed to in the Stipulation. CUB Init. Br. at 66.

K. Refund Allocation

Staff proposes that any refund in this proceeding be made to Nicor Gas customers via the Commodity Gas Charge and the Non-Commodity Gas Charge through an Ordered Reconciliation Factor reflected in the Company's Purchased Gas Adjustment ("PGA") filing. Staff Init. Br. at 13-14; Everson Reb., Staff Ex. 6.0, 8:163-9:172; Everson Dir., Staff Ex. 3.0, 18:346-19:369; Tr. 1290:22-1291:10; Tr. 1297:1-4. Nicor Gas supports Staff's proposal. CUB also "supports Staff's proposal as the most appropriate allocation methodology." CUB Init. Br. at 66.

RESA and IGS state that they object to the refund mechanism proposed by Staff because it is allegedly inequitable in that current transportation customers of Nicor Gas would not receive a refund. RESA/IGS Init. Br. at 3, 9. Instead, RESA and IGS propose that the Commission direct allocation of any refund in the manner utilized by the Commission in Docket No. 01-0706. *Id*. at 9-10. Nicor Gas objects to this eleventh hour proposal because there is no evidence demonstrating that such a refund mechanism is appropriate in this proceeding. Moreover, Nicor Gas did not have the opportunity to test whether the proposal by RESA and IGS is reasonable or determine whether it would impose any unreasonable costs or administrative burdens on the Company. Accordingly, Nicor Gas continues to maintain that Staff's proposal is appropriate as it remains the only refund proposal supported by evidence in this proceeding.

IV. CONCLUSION

The evidence described in the Initial Briefs of Staff and Nicor Gas demonstrates that the Stipulation entered into between Staff and Nicor Gas, which will result in a refund to customers of $64 million, is reasonable and should be approved. The Initial Briefs of the AG and CUB also support Commission approval of the Stipulation, which renders moot all but a few of their claims. However, the Initial Briefs of the AG and CUB fail to rebut Nicor Gas' evidentiary

presentation demonstrating that their claims for additional refund amounts relating to the 2001 storage cycle, the LIFO carrying costs, and the DSS withdrawals are wholly without merit. Accordingly, the Commission should reject the speculative claims of the AG and CUB on these few remaining contested issues. Finally, the Commission should grant any other relief the Commission deems appropriate.

Dated: April 27, 2012

Respectfully submitted,

NORTHERN ILLINOIS GAS COMPANY
D/B/A NICOR GAS COMPANY

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CERTIFICATE OF SERVICE

I, John E. Rooney, hereby certify that I caused a copy of the Reply Brief on behalf of Northern Illinois Gas Company d/b/a Nicor Gas Company to be served upon the service list in consol. Docket Nos. 01-0705, 02-0067 and 02-0725 by email on April 27, 2012.

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